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IN THE SUPERIOR COURT OF THE STATE OF ARIZONA

IN AND FOR THE COUNTY OF MARICOPA

ESTATE OF HELEN H. LADEWIG, on behalf of itself and the class of all persons in the State of Arizona who, during any one of the years 1986 to 1989 paid income taxes to the State of Arizona on dividends paid by corporations whose principal business was not attributable to Arizona, et al.,

Plaintiffs

vs.

ARIZONA DEPARTMENT OF REVENUE and its Director, in his official capacity,

Defendants.

No. TX 97-000075

(Assigned to the Honorable Paul A. Katz)

[Oral Argument Set: September 19, 2005 at 8:30 a.m.]

PLAINTIFFS' RESPONSE TO ARIZONA DEPARTMENT OF REVENUE'S MOTION FOR ORDER AUTHORIZING CORRECTIONS TO OVERPAID CLAIMS

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I. INTRODUCTION.

The Arizona Department of Revenue ("the Department") seeks relief to which it is expressly not entitled under the Settlement Agreement. However, to fully explain all the reasons why the Department is not entitled to relief, a brief recap of the history of the Settlement Agreement in the case is helpful.

After the Arizona Supreme Court in 2001 held that this case could be maintained as a class action, *Arizona Dep't of Revenue v. Dougherty*, 200 Ariz. 515, 29 P.3d 862 (2001), the parties thereafter spent approximately eight months negotiating the Settlement Agreement.[1] This Court gave preliminary approval to that Settlement Agreement on September 24, 2002. At the settlement approval hearing on December 16, 2002, the Department moved this Court pursuant to Rule 23, *Ariz.R.Civ.P.*, for final approval of the Settlement Agreement and presented evidence to establish that the Settlement Agreement was fair, reasonable and adequate to both the State and the class. This Court expressly found that the Settlement Agreement was fair, reasonable and adequate and, over the objections of certain class members, entered final judgment approving the Settlement Agreement on December 19, 2002.

This Court's approval of the Settlement Agreement, and specifically its finding that the Settlement Agreement was fair, reasonable and adequate was appealed. Kamman appealed on the ground, *inter alia*, that the Settlement Agreement was not fair because some taxpayers might receive larger refunds than they deserved while others would receive less than they deserved. The Court of Appeals affirmed this Court's approval of the Settlement Agreement and the Supreme Court denied review.

To calculate refund amounts under the refund formula in the Settlement Agreement, three numbers were needed for each class member for each year 1986 through 1989: Arizona income, Arizona income tax paid and dividends received. Having a firm date for finality of these three numbers for each class member was important to both the class and the Department. The Department's expert staff determined that it would need fifteen months to do everything

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[1]December 16, 2002 Transcript, testimony of Steven Shiffrin, the Department's Chief Tax Advocate, 75:7-12; 104:22-105:3. The Transcript is cited in the format "page:line." The relevant portions of the Transcript are attached hereto as Exhibit "A".

necessary to prepare and review its records to ensure the accuracy of its determination of those three numbers for each class member. Class Counsel, on behalf of the class, agreed to give them as much time as they requested.

Paragraph 8 of the Settlement Agreement thus provided that no later fifteen months after final approval (subsequently March 20, 2004), the Department would send to each of the approximately 785,000 class members a Notice of Dividend Calculation with those three numbers in them and those three numbers would become final for each class member within 45 days unless the class member timely objected:

> 8. **NOTICE OF DIVIDEND CALCULATION**. On or before the Notice of Dividend Calculation date (hereinafter "calculation date" which shall be the first business day after fifteen months have elapsed from the day the Court issues a final determination approving the settlement), the Department shall advise each class member, by first class mail sent to the member's most recent mailing address as reflected in the Department's records, of the Arizona taxable income previously reported, the Arizona income taxes previously paid, and the Reported Dividend amount that the Department will be using for the refund formula calculation for each of the years for which a class member may be entitled to a refund under the Stipulation ("Notice of Dividend Calculation."). . . .
>
> A class member shall have 45 days from the mailing date of the Department's Notice of Dividend Calculation to file a written objection to the correctness of the Arizona taxable income previously reported, the Arizona income tax previously paid and the Reported Dividend amount reflected in the Department's Notice. *The Department's Notice of Dividend Calculation shall set forth the right to object to the correctness of these amounts in the Notice. There shall be no other grounds for objection.* ***If there is no timely objection filed in response to the Department's Notice of Dividend Calculation, the amounts set forth in the Department's Notice shall be final for the calculation of all refunds*** *provided for hereunder for the class member.* Class counsel or other authorized representative of the class member shall be contacted if the Department is unable to resolve a dispute directly with the class member. If the class member and the Department cannot agree on the correct amount, the matter shall be determined by the court pursuant to Paragraph 28 below.[2]

The Department timely mailed all the required Notices by the end of March 2004.[3] It never informed the Court or Class Counsel of any problems meeting the negotiated deadline nor requested any extension of time from the Court. Approximately 5,000 class members filed disputes as required by the Settlement Agreement within 45 days of receiving their Notices. As

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[2]A copy of the Settlement Agreement (without exhibits) is attached hereto as Exhibit "B."

[3]The Notices did not inform class members how much their individual refunds would be, nor could the refund amount be easily calculated by the average class member.

for the remaining 780,000 class members, their Notice determinations became final when they did not file a dispute within 45 days of receiving their Notice. Thereafter, in July 2004, the Department mailed the first installment refund payment to all class members.

Now, almost three years after the Settlement Agreement was finalized, two and one-half years after judgment was entered, more than 15 months after the Notices of Dividend Calculation were delivered, one year after the first installment payment was made, and four months after the Supreme Court denied review, the Department comes to this Court and requests that it be allowed to "correct" the Notices of Dividend Calculation for approximately 3,000 class members whom it contends were "overpaid."

The Department has not, and cannot, establish that all 3,000 affected class members have been refunded more unconstitutional taxes than they paid (with interest). The best the Department could establish is that, *based on the settlement refund formula pursuant to which class members received a refund of only 49.28% of the Arizona incomes taxes paid on dividends received*, the affected class members were "overpaid." The parties and this Court always knew that under the Settlement some class members would receive a refund of more unconstitutional taxes than they paid and some would receive less, but overall the class would be made whole. The Court specifically noted this at the December 16, 2002 approval hearing:

> That formula may result in some taxpayers receiving back more than they paid. That formula might result in some taxpayers receiving less back than they paid. The reason, though, that we went to a formula is what essentially ends up happening is we - - we could have gone another way [Court then describes the alternative of individual proof of claims]

[December 16, 2005, Transcript of Proceedings, 14:19-25 (Ex. "A")] Thus, many of these class members may not have been "overpaid" at all, but rather received a full refund of the unconstitutional taxes they paid. The Department has not provided sufficient information for Class Counsel or this Court to know one way or the other.

Even if the affected class members have been "overpaid" according to the Settlement formula, the Department is not entitled to the relief it seeks on several grounds.

First, the Department's Motion should be summarily denied because it is improper under Rule 7.1, *Ariz. R. Civ.P.*, and violates all notions of due process.

Second, the Department impermissibly seeks to modify the final judgment.

Third, the Department is judicially estopped to assert that overpayments to some class members are unfair.

And finally, granting the motion would be unfair to the affected class members and the class.

II. THE DEPARTMENT'S MOTION SHOULD BE SUMMARILY DENIED BECAUSE IT IS IMPROPER UNDER RULE 7.1 AND VIOLATES THE DUE PROCESS RIGHTS OF CLASS MEMBERS.

According to the clear language of the Paragraph 8 the Settlement Agreement, "***the amounts set forth in the Department's Notice[s] [are now] final for the calculation of all refunds***." In its Motion seeking to change the amounts in approximately 3,000 of those Notices, the Department has violated a basic rule of civil procedure. Rule 7.1(a), *Ariz. R. Civ.P.*, requires that "[a]ll motions made before or after trial shall be accompanied by a memorandum indicating, as a minimum, the precise legal points, statutes and authorities relied on, citing the specific pages thereof . . .. "[4] The Department's Motion simply states that Paragraph 28 of the Settlement Agreement provides the court may enter orders "to effectuate the fair and orderly administration of the settlement" and bases its claim for relief on the unsubstantiated allegation that "[i]t is not fair for a class member to receive a refund overpayment due to a clerical error." [Motion at pp. 2 and 5-6].[5] These bare bones statements are insufficient to constitute a proper motion under Rule 7.1.

Class Counsel and the 3,000 affected class members have no idea what the Department's position is legally or procedurally. Under what rule of civil procedure has the Department moved? Is it a motion for correction of a clerical mistake in a judgment under Rule 60(a) and/or (b)? Is the Department seeking to set aside the judgment or a portion of the judgment under Rule

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[4]Rule 7.1 is applicable in tax court through Rule 2, *Rules of Practice, Arizona Tax Court.*

[5]The Department also bases its claim on Paragraph 16 of the Settlement Agreement, titled "Unforseen Circumstances." The reality of clerical errors was ***not*** an unforseen circumstance. Indeed, the Settlement Agreement contains detailed and carefully negotiated provisions regarding the determination of and the finality of the formula refund amount and provides for a means by which class members could correct errors. Furthermore, the Department is judicially estopped to argue that any overpayment was unfair because it argued to the Court of Appeals that such overpayment ***was*** fair. *See* Section IV, *infra.*

60(c)? If so, under what subsection of Rule 60(c)? Is the Department seeking to invoke a particular power of the court recognized under Rule 23, *Ariz. R. Civ.P.*? A particular power of court recognized under Rule 23, ***Fed.** R. Civ.P.*? If so, what is that power and under what line of authority is this power recognized? Under what theory does the Department claim a unilateral right to change the terms of the judgment at this late date only for overpayments the Department claims to have made to class members but not underpayments to class members? On what legal basis does the Department claim the right to pursue class members to recover for alleged overpayment? Is this a tax collection action? Is it a contract action? Does the Department intend that this Court give it individual judgments against 3,000 class members for the specific amount of the alleged overpayments? Does the Department intend to seek repayment from personal representatives or trustees who have distributed the alleged overpayments to heirs or beneficiaries?[6] Does the Department contend it is entitled to interest? If so, at what rate? The tax underpayment rate? The judgment rate? What does the Department intend to do about state and federal income taxes (including taxes paid to other states) that have been paid on these refunds? The list of questions and issues unaddressed by the Department in its Motion is endless. If the Court grants the Department's Motion, many other issues not addressed either in the Motion or in this Response would need to be resolved by the Court. Under no circumstances would it simply be enough for this Court to allow the Department to "correct claim amounts" as it has requested in its Motion. [Motion at p. 1][7] Even if it were assumed that the Court could grant the extraordinary relief now sought by the Department, due process would require an entire new procedure be devised.[8] However, the judgment precludes such an

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[6]Class Counsel has received phone calls from personal representatives who have distributed the alleged overpayments to beneficiaries and are now concerned about personal liability for funds that they never retained.

[7]The term "claim amounts" is a misnomer since no class members, other than Mrs. Ladewig's estate, have ever made a claim with the Department, much less a claim that needs to be "corrected." The Department determined for each class member what their refund amount would be.

[8]To implement the relief the Department seeks, this Court would, at a minimum, be required to take steps to preserve the due process rights of the class members during the (continued...)

outcome.

In fact, with all due respect to this Court, this Court has still not afforded sufficient due process to these class members in connection with this Motion. The September 19, 2005, hearing does not meet the requirements of due process because the Department has neither properly noticed nor briefed the issues to which the affected class members must respond. Furthermore, although the Court ordered notice to be provided to these class members, it has not required the Department to provide proof of notice to the Court, and some notices may have been returned. Nor has the Court required the Department to inform the Court or Class Counsel (who represent these unidentified parties) of the identity of these class members. This Court is simply allowing these 3,000 class members' adversary to run roughshod over them with no assurance of oversight, notice or representation.

In short, the Department's Motion is wholly improper. It has not provided this Court with any authority whatsoever to support the position that it is entitled to do anything other than pay all class members in accordance with the existing judgment and the existing calculations, much less pursue thousands of class members for alleged overpayments.

The Department's Motion should be summarily dismissed without further argument. Furthermore, the Court should not consider any argument presented by the Department in a Reply memorandum. All 3,000 affected class members have been given notice of the Department's deficient Motion and have been given until August 26, 2005, to file a Response (and many have already filed such responses). An attempt by the Department to use a Reply to explain for the first time the legal or statutory basis, if any, on which it seeks relief against these class members will not cure the due process or Rule 7.1 problems with its Motion.

Despite the fact that the Department has left Class Counsel and the affected class members simply guessing as to what issues should be addressed in a Response, Class Counsel will, nonetheless, set forth a myriad of reasons why the Department is not entitled to redetermine or

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[8](...continued)
Department's determination of any allegedly overpaid amount and preserve each class member's right to assert individualized, personal defenses each may have to the Department's claim to recover any such overpayment from them.

otherwise correct the Notices of Dividend Calculation for the 3,000 class members allegedly overpaid, why the Department is precluded from seeking to collect the alleged overpayments and why the Department must, in fact, continue to pay refunds to those class members according to the terms of the Settlement Agreement.

III. THE DEPARTMENT IMPERMISSIBLY SEEKS TO MODIFY THE FINAL JUDGMENT.

The Department ignores the fact that the Settlement Agreement between the Department and the class, which this Court approved on December 19, 2002, was a final judgment which binds the Department under the doctrines of *res judicata* and collateral estoppel. *Matsushita Elec. Indus. Co., Ltd. v. Epstein,* 516 U.S. 367 (1996) (class action settlement agreement approved by state court precluded litigation in federal court of federal claims released in state court settlement even though state court had no jurisdiction over federal claims); *Cooper v. Federal Reserve Bank of Richmond,* 467 U.S. 867, 874 (1984) ("There is of course no dispute that under elementary principles of prior adjudication a judgment in a properly entertained class action is binding on class members in any subsequent litigation"); *See also* Moore's Federal Practice (3rd ed.), §23.181[2] ("A judgment in a properly maintained class action is binding on all class members, as well as named parties, in any subsequent litigation. The principles of claim preclusion (*i.e.*, res judicata or merger and bar) and issue preclusion (*i.e.*, collateral estoppel) apply"). This Court's judgment was affirmed by the Court of Appeals and review was denied by the Supreme Court.

That Judgment/Settlement Agreement gave finality to the Department's refund calculation determinations for all 3,000 affected class members. Pursuant to Paragraph 8 of the Settlement, each class member had 45 days "to file a written objection to the correctness of the Arizona taxable income previously reported, the Arizona income tax previously paid and the reported dividend amount reflected in the Department's notice [of dividend calculation]." Presumably, none of the 3,000 class members who allegedly received overpayments filed such a dispute. Because no objections were filed, for each of those class members, "the amounts set forth in the Department's Notice shall be final for the calculations of all refunds provided for [under the Stipulation of Settlement] for the class member." *Id.*

Now the Department asks this Court to simply cast aside that term of the Judgment/Settlement Agreement, even though it never brought that provision to the Court's attention in its Motion. The Department cites no authority for the proposition that it may ignore the judgment, apparently believing it is sufficient to claim that it made a mistake and a class member may receive a windfall. This is not even sufficient justification for the IRS to ignore legal limitations on its authority. *O'Bryant v. U.S.*, 49 F.3d 340, 346 (7th Cir.1995) ("although it may seem unjust that the IRS cannot recover its erroneous refund in this case (after all, our holding does give the O'Bryants a windfall), we cannot base our resolution of the issue before us on the equities of a particular factual situation. Congress gave the IRS specifically delineated collection authority, and the IRS must act within that authority"); *Pacific Gas and Elec. Co. v. U.S.*, — F.3d — , 2005 WL 1876167, 8 (Fed Cir., August 10, 2005) (refusing to allow the IRS to recover statutory interest erroneously paid to taxpayer even though "[o]ur decision today results in a windfall for the taxpayer").

The Court does not have the power to grant the relief requested because to do so requires this Court to modify Paragraph 8 of the Judgment/Settlement Agreement so that Notices of Dividend Calculation issued by the Department to the 3,000 affected class members are **not** final even if no objection was ever filed with respect to those Notices. This Court could not have granted it *before* the Settlement Agreement was final much less now. When the Settlement Agreement was presented to the Court for approval, the Court could not modify it because it was constrained by its limited role under Rule 23(e). As the Court of Appeals **held in this case**, "[u]nder Rule 23(e), the tax court could only approve or disapprove the settlement; it was not empowered to rewrite the agreement between the parties." *Kamman v. Estate of Ladewig,* No. 1 CA-TX03-0003, Memorandum Decision at ¶ 9 (citing *Hanlon v. Chrysler Corp.*, 150 F.3d 1011, 1026 (9th Cir. 1998)). Thus, the Motion must be denied as a matter of law.

Furthermore, the Department is not even seeking to treat all class members equally. It is not asking the Court to cast aside that settlement provision for every class member – the Department only wants the provision ignored in those instances where it benefits the Department, not in those instances where it would benefit a class member. For example, it

alleges one class member was "overpaid" $29.27 (according to the settlement formula, not according to unconstitutional taxes he actually paid) and it wants that judgment provision set aside so it can recoup that $29.27 from that class member.[9] Certainly among the other 785,000 class members there is one whom the Department could identify as having been *underpaid* by $29 due to a clerical error. However, the Department has not offered to identify that class member, have the provision set aside for him or pay him an additional $29 refund.

Finally, a class action defendant certainly cannot argue for changing a provision in the Settlement Agreement after final approval (and appeal) where the "problem" it seeks to "fix" was foreseeable by the defendant and could have been prevented by the defendant. The Department states in its Motion that it "could not be reasonably expected to process over 785,000 claims without any clerical errors." [Motion at p. 5] Class Counsel wholeheartedly agrees. Class Counsel foresaw the potential for such errors and provided in Paragraph 8 of the Settlement Agreement for a mechanism whereby class members who discovered such errors in their Notice could seek to have those errors corrected through a dispute process with the Department.[10]

Furthermore, the Settlement contained a negotiated schedule for the finality of the numbers on which the refund calculations were based. The Department requested and received 15 months to take whatever steps it believed were necessary to ensure that its determinations were accurate. If it became apparent that the Department had a scheduling problem and could not run whatever verification tests were necessary to ensure accuracy of its determinations before mailing them, it could have requested relief from the Court on the schedule. Such relief had a built in remedy for the class members – additional interest for the delay. There is no issue that if the schedule had been the problem, the Court could have dealt with the issue. However, the Department

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[9]The class member is identified as "YW4JYRB" on p. 3 of Exhibit 1 to the Affidavit of Thomas McGinnis.

[10]The Settlement Agreement further provided that if the class member and the Department could not resolve the dispute as between themselves, Class Counsel would become involved and handle the dispute on behalf of the class member. That process is still ongoing between Class Counsel and the Department for those class members who acted within the time specified in Paragraph 8 of the Settlement Agreement.

chose not to do so. Instead, the Deparetment is asking this Court to relieve it from its own malfeasance.

Class Counsel has exhaustively examined the class action case law and treatises in connection with the preparation of this Response and has found no cases where a class action Defendant has been excused from its obligations under a settlement agreement which has become a final judgment. There is no justifiable reason to allow the Department to be the first.

IV. THE DEPARTMENT IS JUDICIALLY ESTOPPED TO ASSERT THAT OVERPAYMENTS UNDER THE SETTLEMENT FORMULA ARE UNFAIR.

The Department is judicially estopped to seek relief on the ground that overpayment to some class members is "unfair."[11] Our Supreme Court explained the general principles of judicial estoppel in *Martin v. Wood,* 71 Ariz. 457, 459-460, 229 P.2d 710, 711- 712 (1951):

> The general rule of judicial estoppel is stated in 19 Am.Jur., Estoppel, Sec. 74, p. 712: 'It is a general rule that a party is bound by his judicial declarations and may not contradict them in a subsequent action or proceeding. * * *' The rule is also laid down in 31 C.J.S., Estoppel, § 119, p. 381: 'As a general rule, a party who has assumed a particular position in a judicial proceeding is estopped to assume an inconsistent position in a subsequent proceeding involving the same parties and questions.'

In this case, the parties always recognized that some class members would likely be paid more than that to which they were truly entitled and some class members would likely be paid less, but overall the class would be made whole. This Court expressly recognized this fact when it approved the settlement.

> The Court: That formula may result in some taxpayers receiving back more than they paid. That formula might result in some taxpayers receiving less back than they paid. The reason, though, that we went to a formula is what essentially ends up happening is we - - we could have gone another way [Court then describes the alternative of individual proof of claims]

[December 16, 2005, Transcript of Proceedings, 14:19-25 (Ex. "A")] In fact, one of the objectors, Robert Kamman, specifically opposed the Settlement on this ground. This Court overruled Kamman's objection.

Kamman thereafter appealed on that same ground. As the Department noted in its Response Brief on appeal, "Appellant Robert Kamman ("Kamman") argues that the Settlement

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[11]The Department does not identify to whom such alleged overpayments are not "fair." In truth, such overpayments are not unfair to anyone. *See* Section V, *infra.*

is not fair, adequate or reasonable because some taxpayers may receive larger refunds than they deserve while others will receive less than they deserve (Opening Brief at 5). The record demonstrates that the Department could not accurately determine the refunds due class members based upon tax records." [*Kamman v. Ladewig*, Department of Revenue's Answering Brief at p. 6 (attached hereto as Exhibit "C")] The Department defended against Kamman's appeal on the ground that it did not matter whether some class members received more than they were entitled to because "Kamman failed to present any evidence to show that the Settlement is unfair to the State or that the State's obligations under the Settlement are disproportional to what it receives. The Department presented testimony, however, that the Settlement is fair to the State." [*Id.*, pp 15-16 (Ex. "C")]

The Department prevailed on its argument in the Court of Appeals. Having prevailed on its argument that the Settlement was fair even if the State "overpaid" some class members, the Department is judicially estopped from now arguing to the contrary. *Hrudka v. Hrudka,* 186 Ariz. 84, 92, n. 11, 919 P.2d 179, 187, n.11 (App. 1995)("Essential to the concept of judicial estoppel is the principle that a party 'has gained an advantage--obtained judicial relief--in one action by asserting one position, and that in view of his having gained that advantage, he must accept the burdens of that position in any subsequent litigation'")(citation omitted).

This is particularly true where the Department is not harmed by the overpayment. When this case was settled in 2002, the Department's actual liability was estimated to be as much as $477 million. *Kamman, supra,* at ¶ 20. The parties agreed to cap the Department's liability at $350 million (the "Common Fund Cap," *see* paragraph 6 of the Settlement Agreement, Ex. "B"). Although the Department agreed to pay up to $350 million, the Department estimates the total it will pay under the *Ladewig* Settlement Agreement formula, including the overpayments to date, is only $308.5 million.[12] *See* S.B. 1524, 47th Leg., 1st Reg. Sess., 2005 Ariz. Laws Ch. 333 and House Summary for S.B. 1524, 47th Leg., 1st Reg. Sess., 2005 Ariz. Laws Ch. 333 (May 19, 2005) (as transmitted to the Governor) (attached hereto as Exhibit "D"). Thus, even with all

[12]It bears mentioning that the Department also enjoys the substantial benefit of having that $308.5 million include all the Department's costs of administering the settlement.

alleged overpayments, the Department is still paying less than the maximum it agreed to pay the entire class pursuant to the Settlement Agreement. The Department cannot claim that it is being treated unfairly when it is paying a lesser amount than it agreed to pay.

V. CONTRARY TO THE DEPARTMENT'S UNSUPPORTED ASSERTION, GRANTING THE MOTION WOULD BE UNFAIR TO THE CLASS.

The sole basis for the Department's claim for relief is the unsubstantiated allegation that "[i]t is not fair for a class member to receive a refund overpayment due to a clerical error." [Motion at p. 5-6] However, the Department does not explain to whom such payments would be unfair.

Such alleged overpayments are not unfair to the Department. As explained above, even though the Department's liability was estimated to be as high as $477 million, its liability was capped at $350 million and it will ultimately pay only $308.5 million, even with the alleged overpayments.

Such alleged overpayments are not unfair to the other 782,000 class members. Since the entire settlement amount is under the cap amount, all other class members will receive full refunds under the settlement formula.

Such alleged overpayments are certainly not unfair to the class members receiving them. The parties always anticipated that under the settlement some class members would receive more (and some less) than that to which they were truly entitled.

Thus, the "overpayments" are not unfair to anybody before this Court. Thus, no potential harm can come to the class or to the Department under the terms of the Settlement Agreement by virtue of these alleged overpayments.

On the other hand, granting the Department's Motion and allowing the Department to begin collection actions against 3,000 unsuspecting class members who relied upon the Department's calculations would be horribly unfair. As this Court told the numerous class members present at the approval hearing, "The bottom line is that if you are a member of the class, you can sit back and do nothing and you'll get your percentage of returns." [Transcript, 19:7-9 (Ex. "A")]

First, in its Motion the Department may have led this Court to believe that all of the class

members from whom it seeks repayment have been grossly "overpaid." This is simply not the case. The Department has not established that all 3,000 affected class members have been refunded more unconstitutional taxes than they paid (with interest). At best, they have only been "overpaid" based on a refund of 49.28% of the taxes they paid on dividends received. In any event, most of the "overpayments" are rather modest in amount. Although the Department mentioned in its Motion that one class member was "overpaid" by $1,000,000 and one that was "overpaid" by $17,000, those numbers are misleading. The Department has provided information on only 1,360 allegedly overpaid class members in connection with its Motion. The data shows "overpayments" as small as $29.27 and several less than $200.[13] Furthermore, of the 1,360 allegedly overpaid class members identified in the Motion, 454 (34%) have been "overpaid" less than $1,000 and 478 (35%) have been "overpaid" between $1,000 and $2,000. The remaining 1,670 class members yet to be identified have been "overpaid" less than $1,000 each.[14] Thus, of the 3,000 affected class members, 70% have been "overpaid" less than $1,000 and 16% have been "overpaid" between $1,000 and $2,000 each.[15] A purported payment of one or two thousand dollars in excess of the 49% formula discount is hardly an amount that would lead a class member to believe that the Department had in fact made an error, particularly since it is highly unlikely that they had their tax return information from 15 or 20 years ago.[16] These

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[13]*See, e.g.*, Exhibit 1 to the Affidavit of Tom McGinnis at p. 3 – class member YW4JRB, overpayment $29.27; at p. 7 – class member CPZXBJY, overpayment of $78.80; at p. 14 – class member 4LZMRMF, overpayment $137.41; at p. 19 – class member MWXZZN7, overpayment of $188.44; at p. 21 – class member MRNX4LC overpayment of $72.01; at p. 24 – class member NMFJXP2, overpayment of $154.68; at p. 28 – class member MPWMWFP, overpayment of $78.55.

[14]Although the Department avowed two and one-half months ago that it would provide information to the Court about overpayments to the other 1,640 class members, it still has not done so. However, Department's counsel did avow that the data provided with the Motion was the result of the Department's search for class members who had been "overpaid" by $1,000 or more and that the remaining 1,640 had smaller overpayments. [Transcript of May 26, 2005, 12:10 - 13: 19 (attached hereto as Exhibit "E")]

[15]Ninety-four percent(94%) of the affected class members were "overpaid" less than $4,000.

[16]A formula was used in the settlement of this matter precisely because class members did not have their tax return information. This Court even informed the assembled class members

(continued...)

class members have simply not been "overpaid" an amount which warrants involving them in new proceedings with the Department simply as a result of the Department's unilateral mistake and lack of foresight.

Second, the Department comes to this Court with unclean hands. The Department has always known it would make clerical errors. Indeed, in October 2003, less than five months before it began sending out the Notices to class members, the Department told the Court of Appeals that it anticipated making clerical errors in the calculation process.[17] Nonetheless, instead of seeking a solution to any problem BEFORE the Notices became final pursuant to the Settlement Agreement (such as by requesting an extension of time from the Court to send Notices so it could correct clerical errors or seeking relief before checks were sent), the Department sat on its hands for more than a year. In the interim, the "overpaid" class members cashed the refund checks and spent the money. Only now, at this late date, does the Department tell these class members, out of the blue, that they had no right to rely on what the Department told them, despite the clear language of the Settlement Agreement. The Department should be estopped to do so on equitable grounds. *See, generally Valencia Energy Co. v. Arizona Dep't of Revenue*, 191 Ariz. 565, 959 P.2d 1256 (1998). The objection by a class member attached hereto as Exhibit "F," who is the beneficiary of her deceased brother's estate, highlights this point.[18] Based on the terms of the Settlement Agreement, that class member believed the amount of the refund due her brother's estate was correct and spent the refund accordingly. She has now been told she was over paid $1,400 which she says is "a very substantial amount that would be extremely difficult for me to repay either now or in the future." Her situation certainly cannot

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[16](...continued)
present at the approval hearing that "I'm a lawyer, I'm a tax court judge, I don't have any tax returns of mine that are more than five years old. I threw them away." [Transcript, 15:5-7, Ex. "A"]

[17]In it Answering Brief at p. 9, the Department stated, "The Formula is relatively easy to administer. The only variables are the amount of the dividend income reported on the class member's federal return, the taxable income on the class member's Arizona return, and the tax paid to Arizona. *The most likely discrepancies should be caused by* amended returns filed after 1989 or *clerical errors in keying in the return information.*"(emphasis supplied) *See* Ex. "C"

[18]The personal information about that class member has been redacted from the objection.

be unique among class members.

Third, the Department seeks to retain all of the benefits of the Settlement Agreement (the $350 million cap, the settlement administration costs borne by class members, the finality of any *underpayments* to class member based on clerical errors) while at the same time trying to avoid the burdens that come with the Settlement Agreement, namely the finality of all Notices of Dividend Calculation that were sent to class members. The State cannot take the benefit of the contract and avoid the burdens.

Finally, if the Court grants the Department's Motion, it will violate another provision of the Settlement Agreement. The Settlement Agreement provides that the final payment must be made no later than July 21, 2006. If the Court grants the Motion, the additional resulting litigation will make it unlikely that deadline will be met. Such a result underscores the meritlessness of the Department's Motion.

In sum, while there is nothing at all unfair about denying the Department's Motion and forcing the Department to comply with the terms of the Settlement Agreement, it would certainly be unfair to the affected class members and all the other members of the class for the Court to grant the Department's Motion.

VI. CONCLUSION

For the foregoing reasons, Plaintiffs respectfully request that the Court deny the Department's Motion and further renews its request that the Department not be reimbursed for any administrative expenses incurred in connection with either the Motion or the effort to develop the underlying information needed to file the Motion.

RESPECTFULLY SUBMITTED this 19th day of August, 2005.

BONN & WILKINS, CHARTERED
O'NEIL, CANNON, HOLLMAN, DE JONG S.C.

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ORIGINAL filed and copy hand-delivered this 19th day of August, 2005 to:

The Honorable Paul A. Katz
Maricopa County Superior Court

COPY of the foregoing mailed this 19th day of August, 2005 to:

Lisa A. Neuville
Office of the Attorney General
1275 West Washington
Phoenix, Az 85007

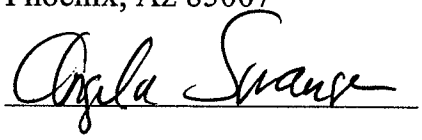

Exhibit "A"

IN THE SUPERIOR COURT OF THE STATE OF ARIZONA

IN AND FOR THE COUNTY OF MARICOPA

HELEN LADEWIG, Plaintiff,	)	
vs.	)	NO. TX 97-000075
ARIZONA DEPARTMENT OF REVENUE, Defendants.	)	

Phoenix, Arizona
December 16, 2002

BEFORE: THE HONORABLE PAUL A. KATZ, Judge

REPORTER'S TRANSCRIPT OF PROCEEDINGS

Bethany D. Campbell, RPR
Certified Court Reporter
Certificate No. 50199

trial in this case, the class members would get whatever percentage or whatever amounts the Court ultimately decided were fair and just under the circumstances.

So what I'm saying to you is if you received the notice that might have been a surprise to you that you might be getting anything back, I can't do the arithmetic for you. But if you don't do anything, and you received notice, you will more likely than not be receiving a refund. It might be small, it might be large and that will be paid off essentially over the next four years.

Just one more note, the settlement agreement that was negotiated by the lawyers on behalf of the plaintiff class and the Assistant Attorney General on behalf of the Arizona Department of Revenue resulted in a formula method being used to pay refunds. That formula may result in some taxpayers receiving back more than they paid. That formula might result in some taxpayers receiving less back than they paid. The reason, though, that we went to a formula is what essentially ends up happening is we -- we could have gone another way.

We could have given you a notice and required each of you class members to opt in; that is to file a proof of claim with this court and to ultimately produce your 1986, '87 '88 and '89 tax returns. I'm a lawyer, I'm a tax court judge, I don't have any tax returns of mine that are more than five years old. I threw them away. I got tired of holding onto them. And absent some big fraud I committed, I can guarantee you that I haven't done that. I don't need those old tax returns and it wouldn't have been fair if I had required all of you to opt in because most of you couldn't prove that you filed the tax returns yet alone that you proved that you paid corporate dividends.

How do we notify the class? The State painfully, at a great deal of expense, reviewed tax returns or a magnetic records of those tax returns of anybody that we believe potentially is a claimant in this case and those people got notice. We also tried to locate heirs and so forth of those people if they are now deceased.

Not everybody in the class got notice, but there will be an opportunity, if they are members of the class, to come forward and to get

So the Department of Revenue will undertake a lot of the accounting work that would otherwise perhaps be left in the hands of private accountants who would have to be paid for out of this class fund or through other sources.

That's an oversimplification of where we're at. The bottom line is that if you are a member of the class, you can sit back and do nothing and you'll get your percentage of returns. If you need to contact plaintiff's counsel who will be representing you and the several hundred thousand members of the class, they would invite you or welcome you to communicate with them by telephone, in person or through written correspondence to the extent necessary.

As of today's date, absent an extraordinary circumstance, you had to either opt out or object. There are, though, mechanisms in place to make sure that if you're someone here that didn't receive a notice or you received your aunt or your uncle or your father or mother's notice, there are mechanisms by which representatives of estates and heirs to that estate will have the opportunity to receive the payment that their deceased would have received

MR. SHIFFRIN: Thank you, Your Honor.

STEVEN SHIFFRIN,

having been first duly sworn, was examined and testified as follows:

DIRECT EXAMINATION

BY MS. NEUVILLE

Q. Mr. Shiffrin, would you state your name for the record.

A. Steven Shiffrin.

Q. And how are you currently employed?

A. I am the chief tax advocate of the Arizona Department of Revenue.

Q. How long have you worked for the Department of Revenue?

A. Since October of 1988, 14 years.

Q. And did you submit an affidavit or a declaration in support of the settlement agreement?

A. Yes, I did.

Q. I believe that declaration talked about a sampling that the Department prepared; is that correct?

A. That is correct.

Q. And can you tell us how many taxpayers were reviewed as part of that sampling?

difficult to even hire enough people to do that kind of work.

Q. If the Department had done that, would they have been able, assuming current budget levels, to do their day-to-day separations with respect to the other taxpayers and still do this return by return calculation?

A. Given current staffing problems, which asked as part of your question, would it be difficult? Yeah, it would be impossible to do anything. But this -- and this would take years and years and years and years and years because our staffing levels have been down dramatically because of the states fiscal crisis.

Q. So fair to say if we had a return by return requirement claim process we would close down the Department of Revenue to all of its other normal functions just to do the claim process?

A. I'm not sure I would say all, but certainly would close down auditing and probably a whole bunch of other things.

Q. Okay. This morning a suggestion was made by Mr. Rasmussen there was haste here racing in 90 days. This settlement didn't come around in 90 days, did it?

A. No, sir. The settlement we started, if I recall correctly, around January and it took us about seven, eight months to negotiate it.

Q. But I want to invite your attention and ask you to look back well over a year ago, the year 2001. And isn't it a fact that you participated in a preliminary settlement discussion with counsel for the class, several representatives of the attorney general's office, several other members of the Department and director Killion to explore a possible settlement before oral argument before the Supreme Court?

A. Yes.

Q. And didn't we share information and identify problems and issues at that time in connection with that preliminary discussion?

A. Yes.

Q. And now isn't it a fact that after the Arizona Supreme Court issued its decision in August of 2001, that you were asked to oversee a preliminary analysis more refined than that initial discussion of what the potential universe of refunds were for a settlement discussion in late September of 2001?

A. I think asked to oversee was to strong a